Transcript of
KushCo Holdings, Inc.
Third Quarter 2021 Earnings Call
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Participants

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Analysts

Vivien Azer – Cowen
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Rob Alexander – Private Investor

Presentation

Operator

Greetings, and welcome to the KushCo Holdings Fiscal Third Quarter 2021 Earnings Conference Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] Please note this conference is being recorded.

I will now turn the conference over to your host, Mr. Najim Mostamand, KushCo's Director of Investor Relations. Mr. Mostamand, you may begin.

Najim Mostamand – Director of Investor Relations, KushCo Holdings, Inc.

All right. Thank you, operator. Good afternoon and welcome to the KushCo Holdings' fiscal third quarter 2021 earnings conference call. A replay of this call as well as a copy of the supplemental earnings slides will be archived on the Investor Relations section of the KushCo Holdings website, ir.kushco.com.

Before we begin, please let me remind you that during the course of this conference call management may make forward-looking statements. These forward-looking statements are based on current expectations that are subject to a number of risks and uncertainties that may cause actual results to differ materially from expectations. These risks are outlined in the Risk Factors section of our SEC filings. Any forward-looking statements should be considered in light of these factors.

Please also note, as a Safe Harbor, any outlook we present is as of today and management does not undertake any obligation to revise any forward-looking statements in the future.

With me on the call today are our Co-Founder, Chairman and CEO, Nick Kovacevich and our CFO, Stephen Christoffersen.

With that, I would now like to hand the call over to Nick. Nick?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thanks, Najim, and thank you all for attending our fiscal third quarter 2021 earnings call. Hope everyone had a fun and safe 4th of July weekend. I know much of the talk around KushCo these past few months has been around our proposed merger with Greenlane. And I'm excited to report that we were making great progress toward closing within our expected timeline of calendar Q3 2021.

So before jumping into our results for the quarter, I wanted to spend some time providing an update on the merger and the important upcoming special meeting of shareholders to approve the merger. Then we'll shift gears to our Q3 financial results before opening it up for Q&A. So with that, let's turn to slide four of the supplemental earnings slides, where we will go over some of the details for the upcoming special meeting.

As you may have seen by now, we have set our Virtual Special Meeting date to Thursday, August 26 at 12pm Eastern Time. All shares held as of the record date of July 1 will be eligible to vote, and you do not need to attend the virtual meeting to vote. In fact, a majority of shareholders vote well in advance, which is why it's important to be on the lookout for the proxy materials that will be arriving in your mailbox either later this week or next week. These proxy materials will have a control number that is needed to submit your vote, which you can do online, by phone or via mail in just a few minutes.

I just want to stress how important it is to vote your shares, no matter how many or how little you own. Without your support and the overall approval needed to consummate this merger, we cannot realize the expected benefits of this merger, which we believe are significant. I won't name all of them but just to name a few of the benefits of the merger, especially to KushCo shareholders.

One, we will create greater scale and a stronger platform for profitable growth, with the combined company expected to generate more than $300 million in calendar 2021 revenue. Two, we expect to reap significant cost saving synergies to the tune of $15 million to $20 million within the first 24 months of closing. Three, we also expect to reap significant revenue synergies, especially cross-selling Greenlane's best-in-class proprietary-owned brand products to our premier customer base of leading MSOs, LPs and brands. And not to mention point number four, we will finally be able to list on NASDAQ retaining the Greenlane name and ticker symbol, which we expect will result in several benefits for our shareholders, including greater liquidity, increased institutional shareholders and additional sell side coverage.

I could go on and on and I'm happy to answer any questions relating to the merger or the meeting in the Q&A portion of the call. But for the sake of time, I'll just mention a couple of more bullets on this slide. The first is that we launched a dedicated transaction website for the merger, which consolidates all of the information that both Greenlane and KushCo have disclosed, as it relates to the merger. It also has a video summarizing the benefits of the merger and a helpful section addressing frequently asked questions. The website URL is www.greenlanekushcotogether.com and I encourage you all to check it out today.

The final thing that I wanted to call on this slide is that we've engaged Morrow Sodali to help with the proxy solicitation process. If you have any questions related to the vote or need any assistance in voting your shares, please contact them at the number and email seen here on the slide. Thank you all for listening to this important announcement and I will now turn to our fiscal Q3 results beginning with slide six.

Starting with revenue, we generated $28.3 million in fiscal Q3, which was down sequentially but up 27% compared to the same period a year ago, and greater than the $27.5 million to $28 million range we pre-announced a few weeks ago. The 27% year-over-year increase was primarily driven by an increase in sales to our existing top MSO and LP customers, as well as the fact that we secured new MSO customers over this period; as we mentioned in the pre-announcement, 24 of our top 25 customers in fiscal Q2 2021 purchased similar products again in fiscal Q3, albeit not requiring the same quantities as they had in the previous quarter.

This lumpiness will continue to be part of our business, given how well we've been able to align with our top operators in North America, who now drive the overwhelming majority of our sales. But it also means that our results over a single quarter are no longer a good proxy for determining the overall progress and success we're experiencing with these customers. That's why our focus remains on retaining and growing these elite customers over time. And on that note, we're encouraged to see revenue from our top 25 customers increase more than 60% year-over-year. And as I said before, it's not just our sales to these customers that are growing, but also the quality of these customers are improving as our book continues to strengthen to include more of the right customers.

Moving now to gross margin. On a GAAP basis, we generated 15% gross margins for the quarter, which is down sequentially but up from the 11% we generated in fiscal Q3 2021. The year-over-year increase was due to the excess and obsolete inventory charges and prepaid inventory write-offs we recognized in Q3 of last year, as part of our 2020 plan to right size the business and get back to positive adjusted EBITDA, which we successfully did following that quarter in Q4 2020.

But looking at margins from a sequential basis, we did continue to experience the uncontrollable shipping delays we and many other importers of goods have been experiencing for the past couple of quarters. Even though the situation has improved somewhat since the end of last year, where we saw record breaking shipments, severe COVID restrictions of the port and a global shortage of containers, virtually all products coming from overseas continue to experience some delays. Fortunately, it has not materially impacted our ability to effectively serve our customers and get them the products they need on time but, as mentioned before, we have seen the increase in freight costs inevitably create a drag on our margins.

In addition, we did experience lower direct material margins on several of our products, especially for vapes, as we're now cycling through some of our higher price inventory, as we've come out with a more aggressive pricing program. This is especially true for some of our newer, big MSO customers who we first onboard with vape but then take time to do the necessary cross selling into higher margin offerings, such as packaging and energy. As we know, cross selling doesn't happen overnight but we are seeing great progress and expect this dynamic to improve in the coming quarters, as we work with our customers to make sure that we're effectively cross-selling them and we work with our vendors to ensure that we're getting the best price appropriate for our scale.

The good news is that while some of these headwinds are largely uncontrollable, we believe we're doing a very good job of controlling what we can control, which is our costs. So moving on to the next bullet of the page, you'll see our cash SG&A decreased from $7.7 million in Q3 2020 and 8.4 million in the prior quarter to just $7.1 million in fiscal Q2 2021. The year-over-year decrease was largely due to reduced consulting expenses and reduced headcount. Even though we have been experiencing temporary headwinds on the margins front, we are more than pleased to continue operating with fiscal prudence in managing our costs, whilst setting ourselves up to grow profitably.

And lastly on the adjusted EBITDA side, we reported a loss of $1.1 million, which represents a significant improvement from the loss of $2.7 million we recorded in fiscal Q3 of last year. The year-over-year improvement was driven by higher revenue and lower cash SG&A as mentioned.

With that, I'd like to turn to slide seven where we break out our sales by our top 25 customers versus the rest of our customer base. Sales to these elite top 25 customers were up by more than 60% year-over-year and as a percentage of overall revenue, grew from 57% in fiscal Q3 of last year to 72% in fiscal Q3 of this year. We are thrilled to have cultivated such an elite customer base over the last several years and believe this position KushCo extremely well to recognize the sustained year-over-year growth, aligning alongside these customers, as they continue to execute on their aggressive growth plans.

Next, we'll look at slide eight, where we break out our sales by geographic market. Once again, we experienced strong growth in both our adult recreational and medical markets. California experienced a nice sequential uptick and was up 22% year-over-year, as we see that market beginning to pick up again for KushCo. Even more impressive is the growth we're seeing out in the Midwest and East Coast. Our sales to Michigan, Massachusetts, and Illinois, all doubled year-over-year, and these markets are continuing to make up a bigger part of our overall revenue. In fact, we generated the highest level of revenue in company history in fiscal Q3 for both Michigan and Massachusetts, as we continue to increase our presence in these fast growing markets by aligning with the key operators in those states.

Turning now to our medical markets, we experienced strong year-over-year growth of 66%, driven in part by substantial growth in Florida, Maryland, New Jersey, New York, Ohio and Pennsylvania. These markets are the next frontier in the expansion of our industry, especially New Jersey and New York, which have both recently legalized adult recreational use, and will commence their programs later next year. And last but not least, we turn to Canada, where the COVID-19 related lockdown there impacted our sales during fiscal Q3. In fact, roughly half of the $4.6 million sequential decline in revenue for fiscal Q3 could be tied to the pullback in Canada. We've been seeing that a lot of the dispensaries there haven't been cycling through inventory as quickly as they thought because there hasn't been as much foot traffic due to the COVID-19 restrictions. As that country fully reopens, however, we do expect to see a pickup.

Next, I'd like to dive into slide nine, which is our revenue by product mix. Vape was up 43% year-over-year to $19.1 million in sales, as we continue to secure large vape orders from our new MSO customers. As mentioned on the last call, once the anticipated Greenlane merger closes, our combined company will become an even more formidable player in the vape market, as we leverage not only our deep relationship with CCELL and experience in the category, combined with Greenlane's 15 plus years of institutional knowledge and experience in the consumer vape category, their unique premium third party brand offering and their diversified expansive customer base.

Packaging papers and supplies was a 12% year-over-year, as our customers continue to expand in both existing and new markets and as we continue to secure and complete higher value custom packaging projects.

And last, I wanted to take a brief look at our Energy and Natural Products bucket, which generated $1.6 million of revenue for the quarter, slightly up from last quarter, but down overall from the prior year period. The year-over-year decline was largely due to the hand sanitizer crisis on Q3 of last year, as several customers shifted their focus to producing sanitizers, which led to a higher level of ethanol sales in the prior year period. Even though those same dynamics from last year don't exist today, we are still gaining traction selling ethanol to our MSO customers, which we ultimately deem more valuable where we're continuing to see strong adoption as well of our stainless steel tanks for butane locking up more and more customers into supply contracts for this differentiated offering.

And with that, I'd now like to turn the call over to Stephen, who will walk us through our Q3 financial summary.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Thanks Nick. I'll now turn to slide 11, which displays a snapshot of our income statement for the quarter. Total net revenue increased 27% year-over-year to 28.3 million. As Nick mentioned, we're continuing to experience strong growth from our MSO and LP customers, which is a part of our strategy to align with the industry's leading operators.

On a GAAP basis, gross profit for the quarter was 4.4 million or 15% GAAP gross margins. As Nick mentioned, gross margins were down sequentially, primarily due to lower material margins, and an increase in freight charges related to shipping delays. We expect gross margins to have these headwinds, especially the lower material margins for a couple quarters, as we cycle through the higher priced inventory. And on the freight side, we're evaluating some options to offset these higher charges, which along with security, more favorable pricing from our vendors should help us return to the mid-20s gross margin levels we know this business can generate.

On a non-GAAP basis, excluding the impact of China trade tariffs, gross profit was approximately $5 million or 20% of revenue. For complete reconciliation of GAAP to non-GAAP financial information, please visit the reconciliation table at the end of this presentation or our fiscal Q3 earnings release.

Sales, general and administrative expense for fiscal Q3 2021 was approximately 9.1 million, which was down 28% from the 12.7 million in fiscal Q3 2020. The big drivers year-over-year were reduced headcount, bad debt expense and consulting spend expenses, largely as a result of the COVID-19 pandemic as well as the implementation of our 2020 plan to right size our business and align it with the leading operators in the industry. Cash SG&A, which excludes non-cash expenses such as bad debt, stock-based compensation, depreciation and amortization was 7.1 million, which was down sequentially year-over-year from the 7.7 million in fiscal Q3 2020.

Turning now to the next item, on a GAAP basis, net loss for fiscal Q3 2021 was $8 million or negative $0.05 per share, which represents an improvement of a net loss of approximately 13.5 million or negative $0.11 per share in Q3 2020. This significant year-over-year improvement was driven by restructuring initiatives, which led to prepaid inventory write offs of $1 million, as well as excess and obsolete inventory charges of 2.1 million in fiscal Q3 2020.

On a non-GAAP basis, excluding the impact of certain non-reoccurring charges, our net loss for the quarter was approximately 3.2 million or negative $0.02 per share, compared to the net loss of 5.5 million or negative $0.05 per share in fiscal Q3 2020.

And finally, adjusted EBITDA for the quarter was negative 1.1 million, compared to the negative 2.7 million in Q3 2020. The year-over-year improvement was due to higher revenue and decreased cash SG&A, as Nick touched on earlier.

As you can see on the next slide, slide 12, we believe the business is becoming a lot healthier with a stronger book of customers, elevated revenue and much smaller losses, as we achieved positive adjusted EBITDA in two of the previous four quarters. We are right on the cusp of achieving that feat again, as we continue to grow revenue and maintain our lean cost structure.

Turning now to slide 13, which provides a snapshot of our balance sheet, as of the end of the fiscal Q3. Our AR for Q3 decreased sequentially year-over-year to 7.4 million, as we continue to generate strong collections activity, especially from some of our smaller customers. In fact, bad debt expense was actually negative for the quarter, as we successfully collected on several doubtful accounts.

Total inventory increased slightly on a sequential basis to 52.4 million in fiscal Q3 2021, with the increase largely driven by inventory purchases and higher freight and tariff costs. We feel really good about our inventory position, especially the quality of the customers that these products are linked to.

Cash during fiscal Q3 was down year-over-year, as we used a significant portion of our $40 million capital raise in February to pay off both our term debt and the balance on our line of credit. I can say it's a tremendous feeling to have virtually no debt on the balance sheet and a healthy amount of working capitals to support our continued grow.

With this strong balance sheet, we're excited to merge with Greenlane, who also has a solid balance sheet with no debt, enabling the combined company to start off on the right foot and be in the best financial position possible.

And with that, I'll now turn it back to Nick.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

All right. Thanks, Stephen. Looking ahead, we are excited to move closer toward consummating our merger with Greenlane and creating the industry's leading ancillary cannabis company and house of brands. As I mentioned at the onset, one of the final milestones left is the shareholder approval required to approve this merger.

And we strongly encourage all shareholders to make their voices heard and to vote their shares using the proxy materials that have been provided to them. We are thrilled by the prospect of joining forces with Greenlane and generating significant value for shareholders. But as I mentioned before, we can't create any of the expected value from the merger until we get the required shareholder approval. So, please vote today.

And with that, I'd like to turn it over to the operator for the Q&A session.

Operator

Thank you. We will now be conducting a question-and-answer session. [Operator Instructions] Thank you. Our first question comes from Vivien Azer with Cowen. Please proceed with your question.

Q: Hi, good afternoon.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Hi, Vivien. Good afternoon. How are you doing?

Q: I'm good. Thank you. So my first question is on the top line, fully appreciate that there's going to be some lumpiness quarter-to-quarter, given the higher concentration around e-customers. That makes a lot of sense. But I'm just curious as you're having the conversations with those top MSOs and LPs, like what sense you're getting around their optimism around post COVID recovery, in terms of kind of consumer spend, the potential impact from incremental stimulus from the child tax credit that kicks in next week? Are you sensing any change in tone from your key partners? Thanks.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah, great, great question. I think one thing is important to know, right, like, our forecasts, a lot of our forecasts, are coming from those customers and so since us being off means that they were off too. So I think certainly sentiment is important but in reality none of us can really predict exactly where those sales are going to be, especially in this climate. I mean, look, I think, in general, as you know, the MSOs are expanding aggressively, organically and inorganically. So we're seeing them bullish on overall growth, in terms of going a little bit more granular, market by market, same-store sales, things like that related to tax credits or other stimulus.

We haven't been having too many of those conversations, at least I haven't, to be able to really comment on that. But I think the general sentiment is, the industry continues to grow these MSOs, believe they're going to continue to grow long-term in their existing markets and expanding into new markets. And so really, if you take the year-over-year view or the lens, it's going to be very bullish across the board and that is consistent with what we're hearing.

And I don't know if Stephen has anything additional to add to that.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Yeah, I was just going to add, maybe, on the Canada front, so you can see in our revenue breakout by location, obviously, Canada down pretty substantially quarter-over-quarter. And that's as a result of the lockdowns, but the word on the Street, at least from our sales directors who are talking with the different buyers at these firms, they're feeling good, and they feel good that they're going to be able to sort of sell down the inventory between now and the end of the calendar year. So, I guess the message there is, there is an end in sight north of the border, so that's encouraging.

Q: No, that certainly is encouraging. Thank you both for that color. Albeit a small market, just a follow up on the revenue line on Nevada, a little bit surprised to see that down again, albeit small, just my impressions from the press is that Nevada is one of the markets where you've seen tourism kind of come back in a pretty encouraging way. Any specific commentary on that market?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

No. Specifically haven't dug in as deep to be able to answer that, but I know, there's a couple of large MSOs that we're doing a significant amount of business with that have had decent presences in Nevada, I would say we probably underperform there in terms of aligning with some of the other larger players that are more single state or smaller multi-state operators.

So there's some opportunity for us to just align with more significant clients in that market, but nothing specifically that we're concerned about with our MSOs that play there. And I think it could be due to some lumpiness that we saw that market kind of come up – come in where it did in Q3, and I haven't looked at our Q4 numbers to date. But I would hope that we're seeing that a little bit of a recovery there for us.

Q: Terrific, thanks. Last one for me. Recognizing the shipping delays are completely outside of your control and are really a global phenomenon that are far from unique to cannabis or US cannabis even. But like, what kind of indicators are you watching for? Or, perhaps more importantly, like, what can we be looking for externally to get a sense that some of that pressure might be easing?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

So, I mean, I think companies are adjusting to it and I think we're going to have to figure out how we can offset some of the impact that we're experiencing and share that with our customers and that's already in motion. We've rolled out a new program where we have very tight customer requests, the timeframes, and if the customer needs a product ahead of that schedule, it's going to require an air shipment, which we continue to do for vape, it's actually not terribly more expensive for vape, just because there's a higher average selling price on those products and their smaller footprint in terms of dimension, versus like a glass jar that's cheap and takes up a lot of space, it's heavy. It really never makes sense to airship that, although we've done that in the past, as you know, Vivien.

But with the air shipping for vapes, specifically, we're offering that but the customer has to then pay the difference, right. So that's something we weren't necessarily doing where we were kind of like, okay, they need it a month earlier and we would sort of eat that. We're moving to a system where we're not doing that now, which will show up in Q4. So little things like that, that we can do to control what we can control. But on the macro front, when this is going to ease up, nothing specifically comes to mind there would be an indicator that the Street could look at to see that start to improve.

I don't know if Stephen has any insight there. Go ahead, Stephen.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Yeah, I mean, we're all sort of following the headlines, as it relates to the trade war and so the tariff impact is probably here to stay. And as Nick mentioned, we have just gotten a little tighter, with the customer requests and trying to pass through some of those costs that they needed earlier. But I think for us really what we're paying attention to and what we'd like to see here in our fiscal Q4 is ultimately that inventory picked up, it picked up incrementally from like 50 to 52 this quarter. We'd like to see that start to come down, which is usually the case.

And so as that happens that basically means that we're sort of – some of the shipping delays have kind of worked themselves out and that business has become a little bit more predictable. I mean, we've got shipments lined up, we're sitting here at early July, we have visibility now kind of what's going to hit between now and call it early September, we feel pretty good about that. So, for us, it’s just kind of a quarter by quarter basis, but definitely something that we need to start reevaluating and potentially passing on to customers.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Well, that reminds me of one of the things that I think is relevant just to expand on this point, because I believe you asked a great question, Vivien. One of the things that we’re kind of wrestling with is as a larger publicly traded company, we do things by the book where we have the tariffs that have been affecting us for years. We also have the shipping headwinds that are really kind of universal. And then you also have this PACT Act, which we had to move everybody over to shipping on LTL and FTL we talked about in the last call.

Currently, a lot of our competition is cutting corners, right. They’re underpaying on the tariffs. They’re still using UPS and FedEx and USPS. USPS, let me just be clear, you can still ship through USPS, although that is expected to close but UPS and FedEx you can’t, people are cutting corners, they’re doing it, they’re getting away with it. These are smaller companies, right. They have less to lose. They’re taking the risks. And so we look forward to a more level playing field and so we’ve been reluctant to pass more of this on to our customers, because we know that the competition is in a better position, not having to pay their fair share of these expenses.

So we’re wrestling with that and we’re seeing actually coming down the pipe, more enforcement, especially with the PACT Act. Also, with the customs and tariffs, we’ve heard whispers that there’s some crackdowns coming. And so we’re expecting that that playing field to be leveled a little bit, which will give us more opportunity to get some of that margin back without risk that some of these smaller, private companies can cut corners and undercut us if and when we do move forward with trying to recoup some of those additional expenses.

So I think that’s an important dynamic to understand long term, we’d rather do things the right way. And ultimately, we think over time, people that are cutting corners aren’t going to be able to continue to build their business in this industry. But we’re dealing with it in real time and we’re making decisions of how much do we look to recoup when we know there’s competition that’s getting away with stuff versus let’s keep our customers happy, let’s keep the competition at bay, and let’s ride through this tumultuous time with all of these regulatory changes, hoping that there will be proper enforcement companies will start to comply, and there will eventually be a level playing field, which will favor us.

Q: Certainly, that seems like a reasonable approach. Thank you both for the color.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thank you, Vivien.

Operator

Thank you. Our next question comes from Aaron Grey with Alliance Global Partners. Please proceed with your question.

Q: Hi. Good evening, and thanks for the questions.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Hi, Aaron.

Q: Hi. How is it going? Just want to go back in terms of the competitive environment and specifically, the pricing. Just wondering, could you give some more color in terms of your new, more aggressive pricing program that you've rolled out and whether or not you're now kind of utilizing that more so in a defensive mechanism as people try to might come after your business and CCELL with specifically those kind of price margin premium or if you're also kind of using it in a more aggressive tactic, and also kind of gaining more business or just if any more color, you could kind of provide there. I know you had been talking about potentially rolling this out for past couple quarters, so. Thank you.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah, great question, Aaron, and we are embarking on a three-prong strategy to do two things right, defend and protect the market that we have, but also to expand and garner additional market share. So pricing is one of the prongs. The pricing strategy that is underway, we see have been very effective in doing both right, defending and expanding our business. So you will see some additional expansion of our market share and see sales market share with that tactic, but it's complemented by two other prongs.

The second prong being innovation, we believe, again, CCELL, the parent company is more, for those who aren't familiar, it's worth almost 40 billion. They've got – they raised a billion in cash in their IPO last year. They're well funded. They've got engineers, upwards of 500, 600, 700; I don't even know the latest number. And they're developing a lot of intellectual property and they're bringing next generation products to market. We see that as obviously a huge barrier to competition, right. We believe that the more we will continue to innovate and be the dominant leader in vapor technology for the foreseeable future, so we feel great about being aligned with them.

And the third prong is a legal strategy. As there is IP developed, we intend and more intend to defend that intellectual property. And so using the three-prong strategy, we're very optimistic that we'll be able to retain the business that we have and retain that for the foreseeable long-term future, but also go out and take new business and hopefully knock out some of the competition that has come in and undercut pricing on products that in our opinion, maybe infringing on intellectual property, right. So we'll see how it all plays out but the three prong strategy we feel very good about. And we're already underway, as you know, with some of those initiatives currently in the market, including the pricing.

Q: Thanks. Appreciate that. That's helpful color. Second question for me, just looking up to Canada, I can certainly appreciate how you had some sales kind of come down sequentially with what we have going out there with the lockdowns are a little more prolonged than here in the US but a little more big picture question. I guess longer term, couple of quarters we had talked about the fact that there was some LPs that might have been – or operators are looking to kind of go for some of the lower pricing options in terms of devices for vapor just because of the pricing pressure in the market.

But OCS came out with a report last week for Ontario that of the complaints that they're receiving about 72% were from vapes, over 9000, just due to quality issue. So was just wondering if you've seen kind of going back, as you're talking to some of these LPs, if they're now looking to maybe be willing to kind of pay a greater premium for a better product, especially on the battery or CCELL side that they don't have these issues and potentially risk getting delisted and whether or not those conversations started to evolve and you've been able to potentially bring out more customers up there. Thanks.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah. Look, Aaron, it's almost as if, what I said, I forget – when I said a while ago, is playing out, right. We saw it happen here in the US and now you're seeing it happen in Canada, right. So you have this big boom in the market, you got all these companies doing well, looking to lower their costs and maximize their profits. As soon as something goes wrong that's when people decide, hey, maybe it's not all about maximizing every dollar of profit, maybe I should be sure that I have a quality product that can scale with my business. That's where we saw in the US a migration specifically for the larger MSOs back to the CCELL platform.

And in Canada, we saw the initial part happen where, again, everybody wants to differentiate, everybody wants to have lowest cost and so there's a proliferation into other, in our opinion, lower quality products. And this is one of the effects that now is showing up in the market. And I do believe it is and will continue to drive more, especially the larger operators, back to the CCELL platform. I know specifically, we work with one of the largest, not the largest – big player in the space using CCELL. Is that why they're leading the way in Canada? I don't know. I would argue it has something to do with it. Are people going to take note of that? Are they taking note of that? I would think so, right.

So I believe the dynamic you laid out is going to happen as you laid it out. And it's one of the reasons why we feel so bullish about our relationship with CCELL and the future performance of the CCELL products in all markets because of the fact they've demonstrated they can produce the highest quality products at the largest scale in the key cannabis market.

Q: Okay, great. Thanks for the color and I'll jump back in the queue.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thank you, Aaron.

Operator

Thank you. Our next question comes from Scott Fortune with ROTH Capital Partners. Please proceed with your question.

Q: Good afternoon and thanks for the question. As far as the MSO customers, you secure newly MSO wins from there. Can you provide a little more color on winning these new MSOs from the competition? And how long does it take, with the new MSO you're on-boarding, new vape at a lower margin per se, but when does that new MSO really inverts to become a more valuable customer and initiate other cross sell opportunity there, as you look out from a longer timeframe.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah, great question. Some of the customers we work with are out there publicly and we don't specifically love to name names, but in general, right, we're sort of working with a majority, but there's a few that we are doing a lot of products with. And specifically, as you can see in our revenue, 67% of it is vape. If we have that, if we're the main vape provider for that MSO, there's going to be big dollars attached to it. So to answer your question, it differs, right.

So one scenario where we on-boarded, I think it was actually in Q2 but on-boarded to one of the top 10, sort of revenue wise publicly traded MSOs, specifically with vape and we're seeing immediate, significant impacts, right. They're one of our top five overall customers, because we started with vape and we're working to diversify and actually win a lot of their packaging business over time.

The flip side of that is we're with a – we just landed a private MSO that started with child-resistant boxes, and we just expanded to providing ethanol. These are great wins, but they're not going to show up really high on the revenue line item, right. So it goes both ways and it depends on how we ultimately land that customer and then how we expand the business with that customer. We're looking at making sure that we're developing good relationships with all of the leading MSOs. We're making sure that we're providing high quality service, right, so they have a great experience with KushCo. We're winning on both of those fronts, right now.

When that actually translates to securing the bulk of their spend and showing up big in our revenue, that we can't control as much but if we do the first thing as well, like I mentioned, ultimately, that revenue will show up. We're not worried about it in terms of ultimately recognizing the value of this strategy but we can't exactly predict when and of course, all of us wanted sooner rather than later. So hopefully that gives you some color on how these things go.

Q: Yeah, and kind of segue. Thanks, Nick. A segue on that business opportunity, have the MSOs started engaging with you more on maximizing their four-wall retail footprint with KushCo and the potential of Greenlane coming on board here as products is add on to purchases within the stores, and then kind of any new initiatives there that you're looking to potentially put in place for the businesses in the fall that we can look forward to, potentially.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah, a great question. And this is really one of the most exciting things about the merger with Greenlane. It is the ability to take their CPG products, bring curated sets hopefully right into these MSO dispensary storefront to help them maximize not only the square footage and the revenue margin in those stores but really, what's most important is that consumer experience, right. Give those consumers the ultimate experience where they can come in, buy their cannabis products, and buy the accessories needed to consume those products in one location, right. So we're super excited about that, unfortunately, until the merger closes, we're not able to action on that. We're planning. To answer your question, Scott, we're planning and we're building a robust plan so that we can hit the ground running and effectuate those cross-selling opportunities.

Greenlane, as a standalone, is not just sitting idle, right. They're winning some of that business. They're slowly starting to build out what they call, currently their enterprise division, targeting dispensaries, and primarily MSO dispensary storefronts. So a little bit of that's happening with Greenlane as a standalone. I don't have direct insight into how much, you'd have to ask them on the next call. But we do know that when the company is merged together, that is the greatest revenue synergy opportunity and so we are doing the planning work to be able to maximize that. We're optimistic.

Some of it is going to be ultimately driven by the market. We know that as the pricing of cannabis comes down and the margins come down, companies are going to look to offset that by offering higher margin higher priced accessories. Of course, we don't want to wait for that. So we'd like to get people ahead of the curve and then we also think that once smart retailers are merchandising properly, they're going to actually differentiate themselves with the end consumer. And if you see, customers walking into someone else's dispensary today have a better selection of cannabis and non-cannabis products, then you're probably going to want to onboard those as well. So there will be some of that ripple effect.

So we're excited to get this going at scale. We believe we're set up to do it really well, given Greenlane's product set and given KushCo's relationships, but we can't really launch that cross-selling program until the merger closes. So hopefully we get the boats in and we can get this thing closed and we can start building that value that we think will be ultimately very accretive for all of our stakeholders.

Q: Appreciate the color. I will jump back in the queue. Thanks.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thanks, Scott. Great question. Appreciate that.

Operator

Thank you. Our next question comes from Eric Des Lauriers with Craig-Hallum Capital Group. Please proceed with your question.

Q: Great. Thanks for taking my questions. First one just a bit of piggyback off that last question. As it relates to that cross-selling opportunity, I understand that it is early stages here. Do you anticipate that that opportunity varying either by customer type, I mean, smaller mom and pop or larger top 25 type customers or do you see it varying by geography at all? You've made some comments on sort of a correlation to the price of cannabis and just wondering if you see it or anticipating it varying by customer type or geography?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah, great question. Thanks for tuning in and asking. I think we're going to learn a lot more once we get in the field. But during the planning work we're doing right now and kind of leveraging the knowledge that we have now, we were talking to customers about theoretical examples. So, I think we have a decent picture. Ultimately, some of it is going to come down to where do we want to spend our resources, so the dynamics are different in each market.

You go to market like Oregon, and yes, the pricing of cannabis has come down and I think retailers are looking to offset or already offsetting that by selling accessories. But it is a much more mom and pop market, not – very little, if any of the MSOs are set up in Oregon with vertical integration into retail.

And vertical integration is the other thing, right. If KushCo is currently doing business with a vertically integrated operator selling products upstream, well, that's a warm channel to open up the downstream retail channels to the Greenlane product set versus going and engaging with a retailer that KushCo is currently doing no business with because they're not vertically integrated, there's nothing to sell them upstream and now this is a brand new relationship that we have to cultivate to sell our product set into their retail footprint.

So where is going to be the best use of our time? What we're thinking right now is going to be leveraging the existing MSOs that are vertically integrated, that KushCo currently has strong relationships with, they are in our top 25, let's just say, right, and having that warm relationship to then penetrate the downstream channel. And because they're an MSO, there's not just one downstream channel, one retail store, right. There's 40, 50, in some cases, upwards of 100 retail stores that we can get access to through one relationship, so that's going to give us the most bang for our buck.

Now, granted, a lot of these MSO footprints may be in markets where the price of cannabis is at its peak and the margins are great on cannabis, there may be a little bit less incentive, so there's going to be a little bit of trade off there, and that's why I think it's a great question you asked. But how we're thinking about it now is where we're going to get the most bang for our buck, it's going to be leveraging the best relationships we have with the largest operators that have the most retail stores. So we're going to start there and then evaluate as it goes.

And obviously, we'll be opportunistic in some of the legacy markets too. And we hope over time that some of that will be consolidated by MSOs and that there'll be a more regional MSOs that that garner larger footprints, and therefore, those same dynamics might be at hand for us to move that strategy into legacy markets.

Q: Okay, yeah, that makes sense. It's a great color there. Thank you. And then just last one, for me, here. Might be a bit of a difficult question to answer, given some of the comments you had on some of these larger customers, sort of starting out with vape, and then getting into more custom packaging and the like. But to the extent that you can provide me color here, could you give us a sense of sort of how much runway you have within your top 25 customer base, within those customers supply and packaging budgets? Like obviously, those top 25 customers have lots of runway ahead of them for growth, but can you give us a sense of sort of your current wallet share and where you think that can go with these customers? Thanks.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah, I mean, look, I think it's a hard question to answer, to quantify even, but we know that the more opportunities that we have to garner additional lines of product, ultimately the more top line that's going to roll up into. So, for example, if somebody – if you look at the top opportunities for KushCo, vape is going to be one of them, vape packaging, but – eight pack – flower packaging, well, eight packaging is probably going to be the biggest one. So if we can land the eight packaging, if we can land the vape packaging, now we've got three of sort of the top five areas of spend, we want to complement that with the ethanol business or butane business, with their concentrate jars, with their pre-rolled joint packs, their pre-rolled joint tubes but there are going to be certain areas and depends on the operator, because some folks that main area for them might be their flower because they're a flower centered brand; others it might be vape because they do vape; others, it might be opportunities with concentrates or pre-rolled joints because they can buy papers, they can buy joint cases.

So it depends on the customer, the MSOs tend to do most of all of it, right. So it is going to be kind of those biggest selling SKUs, right, the bulk of their business, and that's typically going to be especially for fresh vape just because it's higher average selling price. But vape and vape packaging, you know that's a popular SKU and we know when it comes to flower, eight one grant, so we're seeing people go up a little bit to there, they're wanting to have larger quantities available, especially for value line.

So it does depend on the customer and it is hard to quantify, but I always kind of say, within our book, and I think it's equivalent to the top 25, there's probably less opportunity with a third, there's a substantial opportunity with one-third and then there's an even larger opportunity with the other third, probably not relevant for our top 25. But our overall MSO relationships, it's probably a third, third, third, right, where we're doing a lot with a third, there's ample opportunity with one-third and then the bottom third is relatively untapped.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Nick, if may, I can.

Q: Go ahead. Sorry.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Go ahead, Stephen.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

I was just going to take a stab. Yeah, so quantifying the share of wallet, I mean, we have one customer in particular that we have supply contract around and really sticky relationship with. They are not the largest cannabis company out there but there are other cannabis companies that are of equivalent size and scale. And we're doing, it's disclosed around 5 million bucks a quarter with, right, so I mean, that kind of gives you – and that is a relationship that, as Nick mentioned, we've been able to cross sell a bunch of custom packaging and ethanol. So, that's one customer. So the goal here is with the other MSOs in our book, I think it is we proven that we can sell $5 million a quarter to a single customer. There's no reason to think that we can't replicate that with other equivalently sized MSOs.

Q: That's very helpful. Thanks, guys.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thank you.

Operator

Thank you. Our next question comes from Giorgio [indiscernible] holdings. Please proceed with your question.

Q: Hey, guys, how's it going?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Hey, Giorgio, going great. How are you?

Q: I'm doing well. Thank you. My first question for you is regarding the merger and the potential opportunity with increased liquidity and investor awareness going with Greenlane. Do you think that with the current path that you're on and how you've righted the ship as far as

EBITDA and everything else that you would have been able to get on the NASDAQ yourself anyways and Greenlane was just a way to expedite that process.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thanks for the question, Giorgio. I don't know how much we can comment specifically because NASDAQ, our application – we haven't talked much about our application with NASDAQ, other than when we filed it. So, in theory, yes, accelerating it through the merger of Greenlane, getting that size and the scale. I think, also, because of the delay, we publicly announced, we applied for NASDAQ quite some time ago and we were held up and being able to get listed. So the fact that that didn't happen sooner, and we weren't able to garner the liquidity that some of the companies have that they have been able to uplift and do the M&A, that some of the companies have that they have been able to uplift and grow their revenue. Again, merging with Greenlane kind of puts us right back in that same position.

So I think it's twofold, right, the speed and also the size and scale that we get to overnight by effectuating this merger I think is kind of the things we should be considering and the motivation around the listing and doing this Greenlane versus organically.

Q: Absolutely, absolutely. I appreciate you answering their question. My next question for you would be regarding the name Greenway Holdings. Are you wanting to switch that at all or are you happy with the name?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Look, we've announced that we're going to be keeping the name. I personally liked the name. It is obviously something we've discussed we can still consider making a change. But we liked to Greenlane name, I mean, more important, obviously, there's the public side of thing and the name of the ticker. What's really the most important thing for us and always has been at KushCo is the brand reputation in the marketplace, right. If we've got a reputation of servicing our customers well, providing high quality products at great prices, which KushCo has and always has had, we're very grateful for that. We want to make sure that's maintained.

And Greenlane has a similar reputation, right. That was one of the things that in our diligence, we wanted to make sure that their reputation was up there with ours and it certainly is. And so from that standpoint, there's nothing not to like about the name. Could we change your mind? Could there be a scenario where we will look at a different naming strategy? Yes. But for now, we're going forward with Greenlane, GNLN and we believe that the marketplace is excited about that and we will be represented very well with the most important stakeholders, which are customers. And we also want to be cognizant of the marketplace in terms of the listing and the shareholders and that is somewhat of a factor too. But like I said, we haven't made any decisions to deviate from the plan here.

Q: Fair enough. Fair enough. I know, it was a bit of a different question. Sorry about that. My final question for you would be regarding Danny Moses. Is he still going to be an advisor to Greenlane as he is to KushCo right now?

<u>Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.</u>

Good question. We actually disbanded our advisory board, while we went through – after we went through the restructuring. We're still friends with Danny, still confide in him. I mean, he's a mentor, great guy. And we do intend to keep close with Danny, and potentially re-engage him as an advisor at some point down the road. So, keeping our options open, maybe even building that back and other advisory board, at some point. It could be in the future for Greenlane. So, haven't got that far yet but I'm glad you brought that up because Danny has been a great advisor or mentor for the company in years past and continues to be – to play a role unofficially at this point working with me and the company. Yep.

Q: Excellent. The main reason I brought it up is because of Michael Burry's cryptic tweets in the last couple of weeks regarding your company. So I was just curious on the angle there. And Danny Moses was maybe – if they were having some conversations in the background. I don't know if you're familiar with it or not, but your company is blowing up all over Reddit.

<u>Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.</u>

Look, I am familiar with information that's been put out there. I can't comment or confirm how that got out there. I honestly don't even know, right, but yeah, definitely interesting that the Burry is talking about it that the Danny was previously affiliated with the company. Who knows?

Q: Nick, [indiscernible] on the moon, is that the question or what?

<u>Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.</u>

Right. Look, we're flattered that if it is true that Burry is taking a position of the company, we're flattered. We think this is a huge opportunity. We think we're undervalued. We think a lot of smart investors would find value in the company right now. Does that affect how we operate day to day? No. We have a plan, we're executing toward that plan. We want to deliver value to our customers, which will in turn create profits for the company which will deliver value to the shareholders. We're going to stay focused on that. And it's fun to watch but outside of that there's not much that, that really does for us other than creating news.

Q: Nick, I appreciate you answering all the questions. You do me a favor, man. You keep taking those half court shots and go for it, man. You got this.

<u>Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.</u>

Thanks, Giorgio. And we got your email about some Kush bag [ph]. We're going to get that out to you. We know a lot of people are asking for Kush and as we get closer to closing the merger, we might have some extra Kush here to go around for our shareholders. So please do remind that.

Q: Right on, Nick. Thanks a lot, man.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Alright. Thank you. Take care.

Q: Alright. Take care.

Operator

Thank you. Our next question comes from Rob Alexander, Private Investor. Please proceed with your question.

Q: Hey, guys, how you doing?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Hey, doing great. How are you?

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Doing great.

Q: Doing well. Real quick question here. Want to discuss the increase in litigation and consulting costs. I see the 2 million charge down here in the statement this year. I want to see really just how that value adds come back to the company and how this is kind of going to your target market the strategic outcome of this investment?

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Yeah, sure, so we wanted to – so Stephen here. Thanks, great question. This is really tied to the to the merger. So, we lumped it into litigation and consulting, obviously when you effectuate a merger bankers, costs, legal fees, due diligence costs. So, that that's really driving the overall amount of that bucket. So, it isn't that how it's adding value, obviously it's a necessary cost to sort of effectuate a merger but that's really what that is.

Q: Perfect. That is my only question. Appreciate it. I'll go back to the queue.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Hey, really appreciate the question. Yeah.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

All right. Thank you. Najim, do we have any other questions? I am not seeing any in the queue.

Najim Mostamand – Director of Investor Relations, KushCo Holdings, Inc.

No, there are no further questions at this time.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Okay, great. So just coming up on an hour, so we'll wrap up. Thank you guys for tuning in. Really appreciate you jumping on asking the questions. And following the company, there's clearly a lot to be excited about. As we check off these final boxes, leading up to the conclusion of this transformative merger with Greenlane. Today, our industry as a whole is at a critical inflection point. Customers all over are looking to partner with companies that can support their growth for years and decades to come. We believe the combined company, KushCo and Greenlane, will be well positioned to be that premier partner of choice, providing both an enhanced product offering and ancillary services to these customers, while also driving profitable growth for our shareholders.

In my 10 plus years in this industry, I've seen a lot. And I've enjoyed my fair share of excitement but never have I ever been more excited about where the industry is going and more importantly, where KushCo and its shareholders are going than I am right now, with this merger coming down the pipe. We will not only bring together two very complimentary portfolios, which sets us up nicely for the significant cross-selling we talked about earlier, but we will also be serving now an even more elite and diverse customer base going forward spanning across the top MSOs and LPs and leading brands, and also the majority of top smoke shops in the US and millions of consumers directly globally.

We hope that you guys can join us, as we pioneer the next chapter in the cannabis industry and as we work to build a profitable growth engine that becomes one of the few ways for institutional investors to take advantage of the cannabis boom through our NASDAQ listing. So again, thank you all for listening. We hope you all take care, stay safe, and I look forward to providing more updates on the merger in the coming weeks. Cheers.

Operator

Thank you ladies and gentlemen. This concludes today's conference call. You may now disconnect. Have a wonderful evening.